

STATE OF MICHIGAN
COURT OF APPEALS

HANTZ GROUP, INC., HANTZ TAX &
BUSINESS, LLC, HANTZ BENEFITS, LLC,
HANTZ FINANCIAL SERVICES, INC, and
HANTZ AGENCY, INC,

UNPUBLISHED
June 30, 2011

Plaintiffs-Appellants,

v

JASON VAN DUYN, HAROLD PARSLow III,
JONATHAN BAILEY, and AQUEST WEALTH
STRATEGIES,

No. 294699
Oakland Circuit Court
LC No. 2009-101563-CK

Defendants-Appellees.

Before: FORT HOOD, P.J., and DONOFRIO and RONAYNE KRAUSE, JJ.

PER CURIAM.

Plaintiffs appeal as of right from the trial court's grant of defendants' motion to set aside the defaults entered against defendants Harold Parslow III and Jonathan Bailey and the trial court's order dismissing plaintiffs' claims and ordering all parties into arbitration. We reverse and remand.

Plaintiffs' claims arose out of alleged violations of the non-solicitation and confidentiality agreements that defendants signed while in plaintiffs' employ. Hantz Group (HG) offered financial services, including advice and planning. Hantz Financial Services (HFS) was a broker-dealer licensed to sell securities and insurance and was a wholly owned subsidiary of HG. Hantz Tax & Business (HTB) provided tax and business consulting services. Hantz Benefits (HB) provided health care benefits for individual and business clients, and Hantz Agency (HA) provided property and casualty insurance.

Van Duyn was employed by HFS from October 13, 1999, to May 1, 2009. Parslow was employed by HFS from August 6, 2007, to May 1, 2009. Bailey was employed by HTB as an accountant from December 10, 2007, to August 6, 2008. Defendants signed agreements with HG as a condition of their employment acknowledging that HG was providing them with confidential information, that the confidential information was critical to the success of the company and must not be disseminated or used outside of their employment, and agreeing that they would not use the confidential information or disseminate it to any other individual or

entity. Defendants also signed non-solicitation agreements that, for a period of one year after their employment was terminated, they would not contact, solicit, retain, or accept business from any of plaintiffs' clients. Both plaintiffs and defendants agreed that HFS's claims against defendants Van Duyn and Parslow had to be submitted to arbitration under the Financial Industry Regulatory Authority (FINRA). In a stipulated order entered in the trial court, HFS agreed to dismiss all of its claims against Van Duyn and Parslow in the trial court. Defendants failed to file a timely answer to the complaint, and plaintiffs sought and were granted defaults against Parslow and Bailey.

Defendants Parslow and Bailey filed a motion to set aside the defaults against them. Defendants argued that they did not timely file their answer to the complaint because of the ongoing settlement discussion with regard to a breach of contract claim against Van Duyn for repayment of an educational loan and the preliminary injunction sought by plaintiffs. Defendants also argued that their attorney completed and filed the answer as soon as possible. Defendants asserted that, given the amount of damages sought by plaintiffs and the minimal delay in filing their answer, the default would result in a manifest injustice, because the injunction had already been granted. Defendants' affidavit of meritorious defenses averred that the matter belonged in arbitration and that defendants planned to file a motion for summary judgment (sic) pursuant to MCR 2.116(C)(7), demanding arbitration.

At a hearing on the motion to set aside the default, the trial court granted defendants' motion to set aside the default and dismissed all plaintiffs' claims, ordering the case into arbitration. The trial court also denied plaintiffs' motion for reconsideration.

On appeal, plaintiffs argue that the trial court erred in dismissing all of its claims and ordering the parties into arbitration. This Court reviews de novo a circuit court's determination that an issue is subject to arbitration. *In re Nestorovski Estate*, 283 Mich App 177, 184; 769 NW2d 720 (2009).

In the lower court, the parties stipulated to the order for preliminary injunctive relief against defendants. The trial court ordered that all defendants were enjoined from soliciting business from plaintiffs' clients. The trial court also ordered that HFS could only pursue its remaining causes of action against Van Duyn and Parslow in FINRA arbitration. However, the remaining plaintiffs, HG, HTB, HB, and HA submit that they also suffered damages as a result of defendants' violation of the non-solicitation agreements and that they were under no contractual obligation to arbitrate those claims pursuant to FINRA because they were not "members" or "associated persons" of FINRA. Defendants respond that the other Hantz companies were irrelevant and had no valid claims against defendants because defendants Van Duyn and Parslow were only employed by HFS. However, the question of whether HG, HTB, HA, and HB had actionable claims against defendants was not addressed by the trial court. The primary question before this Court is whether the trial court erred in dismissing all plaintiffs' claims against defendants because they were obligated to arbitrate those claims under FINRA.

The existence of an arbitration agreement and the enforceability of its terms are legal questions for the court. *Fromm v MEEMIC Ins Co*, 264 Mich App 302, 305; 690 NW2d 528 (2004). "Arbitration is a matter of contract, and a party cannot be forced to submit to arbitration in the absence of an agreement to do so." *Ehresman v Bultynck & Co, PC*, 203 Mich App 350,

353-354; 511 NW2d 724 (1994). The non-solicitation and confidentiality agreements that plaintiffs based their claims on did not contain arbitration clauses nor does either side argue that they did. The only agreement to arbitrate in this case was based on membership in FINRA. “Each member of FINRA agrees, by membership, to submit to arbitration if a ‘dispute arises out of the business activities of a member or an associated person and is between or among Members; Members and Associated Persons; or Associated Persons.’” *Bank of America, NA v UMB Fin Servs, Inc*, 618 F3d 906, 909 (CA 8, 2010) (citation omitted). “‘Associated persons’ are defined under the FINRA code as individuals who are registered with FINRA, whereas ‘members’ refers to the organizations regulated by FINRA.” *Id.*

HFS is a “member” of FINRA, and Van Duyn and Parslow are “associated persons” of FINRA. Plaintiffs claim, and defendants do not dispute, that plaintiffs HG, HTB, HA, and HB, and defendants AQUEST and Bailey are not “members” or “associated persons” of FINRA. As such, they are not subject to FINRA’s arbitration agreement, and a party cannot be forced to submit to arbitration in the absence of an agreement to do so. *Ehresman*, 203 Mich App at 353-354.

In *Bank of America*, 618 F3d 906, the Eighth Circuit Court of Appeals decided a similar case. UMB Financial Services and the individual defendants appealed the district court’s order declining to compel Bank of America (“BOA”) to submit to arbitration. *Id.* at 908. The individual defendants all worked for BOA as financial advisors, were licensed to broker securities, and also received commissions from Banc of America Investment Services (“BOAIS”). *Id.* The defendants signed non-solicitation clauses, which prohibited them from soliciting BOA customers if they were to leave BOA’s employment. *Id.* All the individual defendants left BOA’s employ and started to work for UMB. *Id.* at 909.

BOA filed suit to enforce the non-solicitation agreements and sought damages. *Id.* UMB and the individual defendants filed a statement with FINRA to commence arbitration proceedings against BOA and BOAIS. *Id.* On appeal, UMB argued that the district court should have compelled BOA and BOAIS to arbitrate in the FINRA proceedings. *Id.* at 910. The Eighth Circuit Court of Appeals held that because BOA was not a FINRA member, it did not directly agree to subject itself to arbitration under FINRA’s terms. *Id.* at 912. Accordingly, the court concluded that defendants had to provide an alternate reason for finding the arbitration agreements were enforceable against BOA. *Id.* The Court further held that state contract law governed the question whether an enforceable arbitration agreement existed between litigants and whether non-signatories could be forced to abide by arbitration provisions. *Id.* This approach has also been adopted in the Sixth Circuit Court of Appeals:

As the district court correctly stated, nonsignatories may be bound to an arbitration agreement under ordinary contract and agency principles. Five theories for binding nonsignatories to arbitration agreements have been recognized: (1) incorporation by reference, (2) assumption, (3) agency, (4) veil-piercing/alter ego, and (5) estoppel. [*Javitch v First Union Securities, Inc*, 315 F3d 619, 629 (CA 6, 2003) (citations omitted).]

In *Bank of America*, the court rejected a theory of incorporation by reference because the employment contracts signed by BOA did not in any way incorporate the FINRA membership

contract arbitration clauses. The court also rejected the estoppel theory because even though BOA's claims were inextricably intertwined with BOAIS's claims under the employment contract, BOA's claims were not inextricably intertwined with the FINRA arbitration agreements. The court held that the defendants had not shown that BOA sought the benefit of the FINRA membership agreements in any way related to the dispute. The court also rejected the third-party beneficiary theory because there was no evidence that the FINRA agreement referenced BOA as a third-party beneficiary or that it contained any language benefiting a third party in BOA's position. *Bank of America*, 618 F3d at 912-914. Ultimately, the court concluded that "the district court did not err when it denied the motion to compel BOA to arbitrate its claims against UMB and the individual appellants." *Id.* at 914. "BOA did not agree in writing or otherwise to arbitrate claims with any of them and cannot be compelled to do so." *Id.*

The facts of this case, like in *Bank of America*, support the conclusion that HG, HTB, HB, and HA did not agree in writing or otherwise to arbitrate claims arising out of the non-solicitation agreements and could not be compelled to do so. The non-solicitation agreements signed by the parties did not incorporate the FINRA membership contract arbitration clauses. Although plaintiffs' claims were inextricably intertwined with HFS's claims under the non-solicitation agreements, they were not inextricably intertwined with the FINRA arbitration agreements. There was no evidence that plaintiffs sought the benefit of the FINRA membership agreements in any way related to the dispute regarding the non-solicitation agreements. The third-party beneficiary theory should also be rejected because there was no evidence that the FINRA agreement referenced HG, HTB, HB, or HA as third-party beneficiaries or that it contained any language benefiting a third party in plaintiffs' position. Accordingly, the trial court erred in dismissing plaintiffs' claims and ordering them into arbitration as they did not agree in writing or otherwise to arbitrate claims arising out of the non-solicitation agreements and cannot be compelled to do so.

Plaintiffs also argue that the trial court erred in granting defendants' motion to set aside the defaults against Parslow and Bailey. This Court reviews a trial court's decision regarding whether to set aside a default for an abuse of discretion. *Alken-Ziegler, Inc v Waterbury Headers Corp*, 461 Mich 219, 223-224; 600 NW2d 638 (1999). It is unclear from the record whether the trial court granted defendants' motion to set aside the default based on a lack of jurisdiction because of the FINRA arbitration provisions or because defendants had shown good cause and a meritorious defense. The trial court simply stated that it was granting the motion and ordering the case into arbitration.

On appeal, defendants argue that the trial court properly granted their motion to set aside the default because the court lacked jurisdiction based on the FINRA requirement to arbitrate. However, as discussed above, plaintiffs, except for HFS, could not be compelled to arbitrate their claims against defendants. Accordingly, the trial court did not lack jurisdiction over the case. In addition, the existence of a valid arbitration agreement regarding a claim does not deprive the trial court of subject matter jurisdiction over the claim. *Campbell v St John Hosp*, 434 Mich 608, 615; 455 NW2d 695 (1990). Accordingly, the defaults should not have been set aside for lack of jurisdiction based on an arbitration agreement between the parties.

A motion to set aside a default can also be granted if the defaulted party establishes good cause and a meritorious defense. MCR 2.603(D)(1). A defaulted party can show good cause by

showing either a procedural defect or irregularity or a reasonable excuse for the inaction that caused the default. *Alken-Ziegler, Inc.*, 461 Mich at 229. The defaulted party's obligation to show good cause and to show, through submission of an affidavit of facts, that a meritorious defense exists are separate requirements. *Id.* The merits of the proposed defense may not be considered when determining if good cause exists to set aside the default. *Id.* at 233-234.

In its motion to set aside the default, defendants did not allege a procedural defect or irregularity. Rather, defendants argued that its failure to file a timely answer should have been excused because of the negotiations that were taking place between the parties regarding the injunction and the breach of contract claim against Van Duyn for the educational loan. In addition, defendants argued that the answer that Van Duyn filed was exactly the same as their answer and, as such, plaintiffs would not suffer any prejudice if the default against Parslow and Bailey were set aside. Defendants further asserted that their attorney completed and filed the response as soon as possible. Defendants argued that, considering the amount of damages sought by plaintiffs and the minimal delay in filing defendants' response, the default would result in manifest injustice to defendants and that, since defendants had already filed an answer, setting aside the default would not result in any prejudice to plaintiffs.

The Supreme Court has cautioned appellate courts not to substitute their judgment in matters within the discretion of the trial court, and has insisted upon deference to the trial court in such matters. *Alken-Ziegler, Inc.*, 461 Mich at 228. Because it appears that the trial court based its decision to set aside the defaults for lack of jurisdiction due to the arbitration agreements, as evidenced by it ordering the parties into arbitration, and because of the deference due to the trial court's exercise of discretion with regard to this decision, we remand this matter to the trial court to make a decision on the record applying the requirements of MCR 2.603(D)(1) to defendants' motion to set aside the default against Parslow and Bailey.

This Court reverses the order sending all the parties' claims to arbitration and remands for clarification of the basis for the trial court's decision to set aside the default and for other proceedings consistent with this opinion. We do not retain jurisdiction.

/s/ Karen M. Fort Hood
/s/ Pat M. Donofrio
/s/ Amy Ronayne Krause